IN THE UNITED STATES BANKRUPTCY COURT

FOR THE

SOUTHERN DISTRICT OF GEORGIA
Dublin Division

IN RE:	)	Chapter 7 Case
	)	Number 96-30671
TIMOTHY HEATH SPIVEY	)	
	)	
Debtor	)	
_____	)	
	)	
SCOTT J. KLOSINSKI, TRUSTEE	)	FILED
	)	at 10 O'clock & 50 min. A.M.
Plaintiff	)	Date: 3-16-98
	)	
v.	)	A d v e r s a r y Proceeding
	)	Number 97-03019A
BANK OF DUDLEY	)	
	)	
Defendant	)	
_____	)	

ORDER

The Trustee in this bankruptcy case, Scott J. Klosinski, filed this adversary proceeding on September 15, 1997 for turnover of property of the estate in the possession of the creditor, Bank of Dudley (hereinafter "Bank"), and for a determination of the extent of the Bank's interest in the property. Turnover of the property to the estate is granted to the Trustee as a priority interest holder, because the Bank holds no security interest in the property.

The parties to this adversary have filed a joint

"Stipulation of Facts." In summary, On April 4, 1995, Debtor and Marsha Spivey executed a combined Promissory Note and Security Agreement in favor of the Bank for $7,500.00. The agreement was submitted as an exhibit with the stipulation of facts; however, the second page was found to be illegible. Debtor pledged a 1991 Chevrolet Silverado he owned as security for the note. The security interest of the Bank was reflected on the Georgia certificate of title for the Chevrolet. On October 4, 1996, Debtor went to the Bank and stated that he wanted to sell the Chevrolet and purchase a 1994 Suzuki motorcycle. Debtor stated that he would not pay off the original loan, but instead wished to substitute the collateral on the note, the Chevrolet, with the Suzuki. The Bank agreed to the exchange. On October 4, 1996, the Bank crossed out the description of the Chevrolet on the original April 4, 1995 security agreement; wrote a description of the Suzuki under the crossed out lines; and Brenda H. Sterling, an officer of the Bank, wrote her initials next to the inserted description. Debtor did not sign or initial the change.

The Bank released its security interest in the truck on October 4, 1996, as shown in a copy of the certificate of title. On the same day Debtor signed a Georgia MV-1 application for a certificate of title for the Suzuki and a certificate of title was issued showing the Bank as first lienholder. Debtor did not sign any other writing to consent to the substitution of the collateral, and Mrs. Spivey did not consent to the substitution

in writing or orally. Mrs. Spivey owns no interest of record in the Suzuki.

Debtor filed this Chapter 13 bankruptcy petition on December 5, 1996. The Bank filed a secured claim dated January 14, 1997. The Chapter 13 case was converted to Chapter 7 on April 15, 1997. The Bank obtained possession of the Suzuki on June 24, 1997. A discharge was entered on July 31, 1997. The Trustee filed this adversary on September 10, 1997.

The Trustee asserts the Suzuki is property of the bankruptcy estate and should be turned over to him under 11 U.S.C. § 542 due to the Bank's failure to create a valid security interest in the substituted collateral. Further, the April 4, 1995 security agreement predates the purchase of the Suzuki, and without the Debtor initialing or signing for the substitution of collateral, the Bank does not hold a valid security interest in the Suzuki. The Bank claims a perfected legal or equitable security interest and lien on the Suzuki, so that the Trustee's request under the complaint must be denied. The Bank argues its security interest is valid because it has possession of the Suzuki, which is one of the three factors to fulfill the attachment requirement of a security interest, and the interest is perfected by its inclusion as a first lien creditor on the certificate of title; the Suzuki amounts to proceeds of the original collateral, the Chevrolet; or the Bank and Debtor both intended the Suzuki to serve as collateral on the original

security agreement. The issue for determination is whether the written-in substitution of collateral on the pre-existing combined note and security agreement with only an officer of the creditor initialing the change suffices under Georgia law to create a security interest for the Bank in the substituted collateral, the Suzuki. It does not.

Section 9-203 of the Uniform Commercial Code, O.C.G.A. § 11-9-203,[1] applies to determine whether a change in a security agreement is valid. The Trustee bears the initial burden of proving property of the estate under § 541, R.H. Williams v. American Bank of Mid-Cities, N.A. (In re Williams), 61 B.R. 567 (Bankr. N.D. Tex. 1986), and demonstrating the invalidity of the security interest. Krigel v. Drake (National Marine Sales & Leasing, Inc.), 79 B.R. 442, 450 (Bankr. W.D. Mo. 1987), citing Matter of Bergsieker, 30 B.R. 757, 759 (Bankr. W.D. Mo. 1983). Neither Georgia state or federal court decisions shed light on

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[1]O.C.G.A. § 11-9-203. Attachment & enforceability of security interest; proceeds; formal requisites. [Applicable Text]

(1) Subject to the provisions of Code Section 11-4-208 on the security interest of a collecting bank, Code Section 11-8-321 on security interests in securities, and Code Section 11-9-113 on a security interest arising under the article on sales (Article 2 of this title) a security interest is not enforceable against the debtor or third parties with respect to the collateral and does not attach unless:

(a) The collateral is in the possession of the secured party pursuant to agreement, or the debtor has signed a security agreement which contains a description of the collateral and in addition, when the security interest covers crops growing or to be grown, a description of the land concerned; and

(b) Value has been given; and

(c) The debtor has rights in the collateral.

determining whether the Bank obtained a security interest in the Suzuki. See generally, In re Couch, 5 U.C.C. Rep. Serv. 255 (M.D. Ga. 1968) (A security agreement signed in blank without a description of the collateral is void and does not transfer a security interest to the creditor). The Supreme Court of Wisconsin, interpreting its own similar version of O.C.G.A. § 11-9-203, analyzed similar facts in Milwaukee Mack Sales, Inc. v. First Wisconsin Nat'l Bank of Milwaukee, 93 Wis.2d 589, 287 N.W.2d 708, 28 U.C.C. Rep. Serv. 540 (1980).

> On November 25, 1975, for valuable consideration, the debtor executed a Chattel Security Agreement to the Bank in respect to the two trucks purchased by the debtor in August and September....The Bank then unilaterally amended the Chattel Security Agreement which the debtor had executed on November 25, 1975, by adding to the agreement the serial number of the third truck. No one on behalf of the debtor signed the agreement after the amendment made by the Bank.
> On March 29, 1976, the Bank filed with the Motor Vehicle Department a Notice of Security Interest Perfection for each of the three vehicles and the three unencumbered certificates of title. The notices referred to the Bank's November 25, 1975, Chattel Security Agreement. The Bank received a certificate showing that the First Wisconsin National Bank was a secured party covering "a 1976 Mack tractor... WS86LST26350,: the third vehicle purchase by the debtor....[W]e conclude that the Chattel Security Agreement dated November 25, 1975, was a nullity in respect to the third truck, because the description of that truck was added to the agreement unilaterally and no officer of the debtor signed that agreement, as is required by sec. 409.203(1) (a), Stats., subsequent to the amendment....[E]ven though the perfection of a security interest in a motor vehicle may be governed by the provisions of the title

> statutes, the creation of the security interest is governed by the Commercial Code....[N]o security interest arose as a result of that document, because the unilateral amendment to include the third truck's description was not followed by a signing on behalf of the debtor, as required by sec. 409.203(1)(a), Stats. That subsection provides that a security interest is not enforceable per se unless "the debtor has signed a security agreement which contains a description of the collateral," and otherwise conforms to the statutory requirements.

Id. See also In re Dykes, 20 U.C.C. Rep. Serv. 524, 1976 WL 23642 (Bankr. E.D. Tenn. 1976) (Interpreting the same U.C.C. provisions, the court held a security interest was not created when a creditor lined out one automobile and added a new automobile to a security agreement and a certificate of title for the new collateral listed the creditor as first lienholder, because the debtor's original signature failed to suffice for a signature for the change when he did not sign for the change).

In similar circumstances, the debtor executed a security agreement for two jeeps on November 21, 1967, a certificate of title was issued, and the security interest perfected. Upon the parties agreement, the jeeps were released and substituted for two other vehicles on February 4, 1969 and March 27, 1969. The creditor typed in the new vehicles on the original security agreement and an officer of the creditor initialed the changes. Certificates of title were issued showing the creditor as a first lienholder on each of the substituted vehicles. The court found a clear indication from the notation on the original security

agreement and the certificates of title the parties intended the security agreement to constitute an agreement necessary to create a security interest. However, without a substitution of collateral provision in the original security agreement, the substitution had to be viewed as an original undertaking. Therefore, the intent of the parties had no bearing on the result and the initialing by the creditor's officer of its change on the security agreement did not create an original security agreement for the substituted collateral. The creditor held no security interest in the two substituted vehicles. In re McTerry Corp., 8 U.C.C. Rep. Serv. 108 (D. Conn. 1970).

The Bank's substitution of the Suzuki on the original security agreement for release of the Chevrolet falls under the same fact pattern as analyzed by the courts above. The Chevrolet was crossed out, the Suzuki description written in, an officer of the Bank initialed the substitution, and Debtor did not sign or initial the change on the security agreement. Pursuant to the foregoing cases the failure of Debtor to initial the security agreement renders the security agreement void and the security interest does not exist. Therefore, the Trustee has shown that the Bank failed to obtain a valid security interest based upon a "written signed security agreement containing a description of the collateral" as required by O.C.G.A. § 11-9-203.

The Bank's argument that the intent of the parties to form a security interest creates a valid security interest for the

Bank is also of no avail, in light of the holding in In re McTerry, 8 U.C.C. Rep. Serv. 108, as previously discussed. Clearly the Debtor intended to grant a security interest in the Suzuki to the Bank because Debtor signed the Georgia MV-1 application for a certificate of title listing the Bank as lienholder. The Bank also intended a security interest as evidenced by its initialing of the change in the original security agreement. However, under In re McTerry, 8 U.C.C. Rep. Serv. 108, the intent of the parties does not create a security interest if the security agreement does not provide for the substitution of collateral within its text. No such provision is included in the April 4, 1995 security agreement.[2] The grant of the security interest in the Suzuki must be viewed as an original undertaking, so Debtor must sign a security agreement to create the interest. Debtor failed to do so. No security interest exists.

The intent argument also is irrelevant by 11 U.S.C. § 544.[3] This provision gives the trustee rights and powers of a

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[2]The second page of the April 4, 1995 combined security agreement and promissory note was illegible. Upon notifying the parties that a legible copy was needed neither party was able or would produce one. The trustee relied upon the legible part of the document to determine whether a valid security interest was created in the substituted collateral, and I also rely alone on the legible wording. No substitution of collateral clause exists on the legible part of the document. The trustee has met his burden of showing the creditor does not have a security interest due to the lack of Debtor's initialing or signing the change.

[3]11 U.S.C. § 544. Trustee as lien creditor and as successor to certain creditors and purchasers.
(a) The trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee or of any

hypothetical judgment lien creditor without notice. The intent of the Debtor to the extent that the Bank seeks to impute that intent to the Trustee is irrelevant.

Bank's argument that it has a valid security interest because it possesses the Suzuki is incorrect. Upon the debtor's filing bankruptcy an estate is created under 11 U.S.C. § 541, which includes any interest of the debtor in property. Furthermore, a stay is created pursuant to 11 U.S.C. § 362 so that all applicable entities are estopped under subsection (a)(3) from "any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate." Debtor had a legal interest, ownership, in the

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creditor, the rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by—

(1) a creditor that extends credit to the debtor at the time of the commencement of the case, and that obtains, at such time and with respect to such credit, a judicial lien on all property on which a creditor on a simple contract could have obtained such a judicial lien, whether or not such a creditor exists;

(2) a creditor that extends credit to the debtor at the time of the commencement of the case, and obtains, at such time and with respect to such credit, an execution against the debtor that is returned unsatisfied at such time, whether or not such a creditor exists; or

(3) a bona fide purchaser of real property, other than fixtures, from the debtor, against whom applicable law permits such transfer to be perfected, that obtains the status of a bona fide purchaser and has perfected such transfer at the time of the commencement of the case, whether or not such a purchaser exists [and has perfected such transfer].

(b) The trustee may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim that is allowable under section 502 of this title or that is not allowable only under section 502(e) of this title.

Suzuki upon the commencement of the bankruptcy case. The Suzuki is property of the estate under 11 U.S.C. § 541(a)(1).[4] The Bank obtained possession of the Suzuki post-petition without obtaining relief from stay as required by 11 U.S.C. § 362(d). The Bank is in violation of the stay. Any stay violation is void ab initio. In the Matter of Newton, Chapter 13 Case Number 96-41369, Adversary Proceeding Number 96-4131, slip op. at p. 8 (December 19, 1996) (Davis, J.). The Bank does not therefore hold a security interest by possession.

The Bank's final argument that the Suzuki constitutes proceeds of the Chevrolet, thus continuing a security interest, also fails. Georgia law defines "proceeds" under O.C.G.A. § 11-9-306(1) to include "whatever is received upon the sale, exchange, collection, or other disposition of collateral or proceeds. ...Money, checks, deposit accounts, and the like are 'cash proceeds.' All other proceeds are 'noncash proceeds.'" A creditor who releases its security interest in collateral eliminates its security interest in that collateral and its proceeds. Ray's Mobile Home Repair Serv., Inc. v. Presidential Fin. Corp., 192 Ga. App. 682, 386 S.E.2d 48 (1989). The Bank can not claim an interest in the Chevrolet or proceeds from it because any interest

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[4] 11 U.S.C. § 541(a)(1). Property of the estate provides in relevant part:
(a) The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:
(1) . . . all legal or equitable interests of the debtor in property as of the commencement of the case.

the Bank had in that collateral was released. Therefore, the Bank gave up any rights to claim an interest in the proceeds which flowed from the sale of the Chevrolet upon its own release.

It is therefore ORDERED that the Trustee's complaint for turnover of the Suzuki is granted. The Bank of Dudley holds no security interest in the Suzuki motorcycle.

JOHN S. DALIS
CHIEF UNITED STATES BANKRUPTCY JUDGE

Dated at Augusta, Georgia
this 15th day of March, 1998.